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No. 97-1685

In the Supreme Court of the United States

OCTOBER TERM, 1997

LANE S. HOWELL, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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14 pp

QUESTION PRESENTED

Whether petitioner was responsible for paying over to the United States federal taxes withheld from the wages of employees of Northern Outfitters, Inc., and willfully failed to do so, and is therefore liable for the amount of the unpaid taxes under 26 U.S.C. 6672.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A1-A11) is unpublished, but the decision is noted at 133 F.3d 933 (Table). The opinion of the district court (Pet. App. B1-B12) is not yet reported.

JURISDICTION

The judgment of the court of appeals was entered on January 13, 1998. The petition for a writ of certiorari was filed on April 13, 1998. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. John T. Dunlop was majority shareholder of a clothing company named Northern Outfitters, Inc.,

and of a holding company named Bonnevest, Inc., which provided management and financial services to its controlled companies (Pet. App. A4). In 1989, petitioner joined Bonnevest as a consultant. In that capacity, he helped to manage various Bonnevest-held companies and Northern Outfitters (*ibid.*). By December 1989, petitioner had been made executive vice president and chief operating officer of Bonnevest. He had also become a director and shareholder of Bonnevest (*ibid.*). He thereafter served two terms as president of Northern Outfitters and was a director of that company from early 1990 until February 1992 (*id.* at B9).

Petitioner first served as president of Northern Outfitters during early 1990 (Pet. App. A5). David Stettler succeeded petitioner as president in June 1990, but he left the company in December of that year (*ibid.*). During the period that Stettler was president, petitioner provided consulting services to Northern Outfitters but had no role in its day-to-day operations. Northern Outfitters failed to remit to the Internal Revenue Service the federal employment and income taxes that it witheld from the wages of its employees during the last quarter of 1990 (*id.* at B6).

In January 1991, petitioner again became president of Northern Outfitters.[1] At that time, petitioner knew that the company had not paid its payroll taxes for the fourth quarter of 1990 (Pet. App. A5). Petitioner testified that he gave instructions to the company's accountant as to which creditors were to

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[1] Bankruptcy disclosure statements filed by Northern in April 1991 state that petitioner had been president since January 1, 1991. Petitioner testified that he took office as president during the second half of January 1991 (Pet. App. A5 n.2).

be paid. He acknowledged that, as president, he had the authority to see that back taxes were paid (*id.* at A7). Petitioner directed the company's accountant, however, to pay only the amount of back taxes set out in the company's operating plan (*ibid.*). When Northern Outfitters filed its Employer's Quarterly Employment Tax Return for the fourth quarter of 1990 on January 31, 1991, the company failed to pay the taxes shown to be due on the return (*id.* at A5). During petitioner's second term as president, accruing payroll taxes were kept current and some payments were made toward the arrearage in the withholding taxes for the fourth quarter of 1990 (*ibid.*). By April 1991, however, the company's financial condition deteriorated to the point that it filed a petition for reorganization in bankruptcy (*ibid.*). Petitioner continued to serve as president of Northern Outfitters until February 1992, when he resigned (*ibid.*).

2. The Internal Revenue Service made assessments under 26 U.S.C. 6672 for the amount of unpaid withholding taxes owed by Northern Outfitters for the fourth quarter of 1990. An assessment of $27,025 was made against Stettler, and an assessment of $38,996 was made against petitioner and Dunlop (Pet. App. A4, B2). Stettler paid $5000 in partial satisfaction of the assessment and brought this suit for refund in the district court. The United States counterclaimed for the remaining amount of the taxes due and joined petitioner and Dunlop in the action. The claims against Stettler and Dunlop were subsequently settled (Pet. App. A4).

The district court granted summary judgment to the United States against petitioner. The court concluded that petitioner was, as a matter of law, re-

sponsible for the payment of withheld taxes owed by Northern Outfitters and had willfully failed to pay over to the United States the taxes withheld from the wages of that company's employees for the fourth quarter of 1990 (Pet. App. B1-B11).

3. The court of appeals affirmed. The court noted that petitioner's own admissions established that he had effective power to pay the taxes when they came due. The court concluded that he was therefore responsible for paying over the withheld taxes as a matter of law (Pet. App. A7). The court explained that it was not a defense that petitioner was not president during the fourth quarter of 1990, when the taxes were collected, for he became president (and thus responsible for paying over the taxes) before the taxes were due to be paid to the United States on January 31, 1991. The court pointed out that the existence of the power to pay over the taxes, once collected, was sufficient to establish responsibility under Section 6672 (Pet. App. A8, citing *Slodov* v. *United States*, 436 U.S. 238, 246-50 (1978)).

The court further concluded that the failure of petitioner to pay over the payroll taxes was willful within the meaning of Section 6672 (Pet. App. A9). The court observed that, when petitioner began his second term as president, he was aware that the payroll taxes for the fourth quarter had not been paid and nevertheless directed that other creditors be paid first, before the outstanding taxes were paid (*ibid.*). The court noted that the company had sufficient funds during this period to pay the delinquent taxes. The company's balance sheet as of December 31, 1990, revealed a cash balance of $27,835.01, its cash on hand as of January 31, 1991, was $11,432.94, and, during January 1991, $93,000 was deposited into its checking account (*id.*

at A10). The court rejected petitioner's contention that, under this Court's decision in *Slodov* v. *United States*, *supra*, he was not liable for paying taxes out of funds received after he assumed office (Pet. App. A10):

> Contrary to [petitioner's] characterization, these were not "after-acquired" funds vis-a-vis Northern. These funds were acquired by Northern and available to it in time to avoid delinquency. The funds were not acquired after the delinquency arose. Unlike Dr. Slodov, [petitioner] did not inherit a payroll tax fait accompli when he resumed duties as Northern's president. When he took over, [petitioner] knew of the outstanding tax liability and had access to sufficient corporate funds to pay it in a timely fashion.

Because of these critical factual distinctions, the court concluded that "*Slodov* does not apply" to this case (Pet. App. A11).

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is therefore not warranted.

1. The status, duty, and authority of a corporate employee determine whether he is responsible under Section 6672 of the Internal Revenue Code for paying over withholding taxes owed to the United States. *E.g.*, *Taylor* v. *IRS*, 69 F.3d 411, 416 (10th Cir. 1995); *Denbo* v. *United States*, 988 F.2d 1029, 1032 (10th Cir. 1993). The focus of this inquiry is on whether the individual has significant control or authority over the enterprise's finances or general decision-making. *E.g.*, *Bradshaw* v. *United States*, 83 F.3d 1175, 1178

(10th Cir. 1995), cert. denied, 519 U.S. 928 (1996); *Denbo* v. *United States*, 988 F.2d at 1032. Of particular concern is the individual's role in corporate financial matters and the power to direct corporate expenditures. See, *e.g.*, *Quattrone Accountants, Inc.* v. *IRS*, 895 F.2d 921, 927 (3d Cir. 1990); *United States* v. *Vespe*, 868 F.2d 1328, 1332 (3d Cir. 1989). The central question is whether the individual possesses the "*effective power*" to pay the taxes owed by the corporation. *Howard* v. *United States*, 711 F.2d 729, 734 (5th Cir. 1983). See *Denbo* v. *United States*, 988 F.2d at 1033; *Ruth* v. *United States*, 823 F.2d 1091, 1094 (7th Cir. 1987); *Neckles* v. *United States*, 579 F.2d 938, 940 (5th Cir. 1978).

Examining the relevant factors in this case, the court of appeals correctly held that petitioner was a responsible person of Northern as a matter of law. Petitioner assumed the position of president of Northern in January 1991, before the fourth quarter taxes were due to be paid on January 31, 1991. It is undisputed that, as president, petitioner had the authority to direct that the United States be paid the taxes withheld from the wages of Northern's employees during the fourth quarter of 1990. On these facts, the court of appeals correctly held that petitioner was responsible as a matter of law under Section 6672 of the Code to pay over the withheld taxes to the United States. See *Denbo* v. *United States*, 988 F.2d at 1033; *Ruth* v. *United States*, 823 F.2d at 1094; *Howard* v. *United States*, 711 F.2d at 734.

2. The court of appeals also correctly held that petitioner's failure to remit the withholding taxes due the United States was "willful" as a matter of law. It is well established that, for purposes of Section 6672, a "willful" failure to remit withheld taxes is estab-

lished by evidence of a "voluntary, conscious and intentional decision to prefer other creditors over the Government." *Denbo* v. *United States*, 988 F.2d at 1033, quoting *Burden* v. *United States*, 486 F.2d 302, 304 (10th Cir. 1973), cert. denied, 416 U.S. 904 (1974). When, as in this case, a responsible person directs that funds of the corporation be paid to other creditors when he has knowledge that withholding taxes owed to the United States have not been paid, his conduct is willful as a matter of law. *Bowlen* v. *United States*, 956 F.2d 723, 729 (7th Cir. 1992); *Olsen* v. *United States*, 952 F.2d 236, 240 (8th Cir. 1991); *Howard* v. *United States*, 711 F.2d at 735; *Mazo* v. *United States*, 591 F.2d 1151, 1157 (5th Cir.), cert. denied, 444 U.S. 842 (1979).

3. Petitioner errs in contending (Pet. 9-12, 21-23) that the decision in this case conflicts with the decision of this Court in *Slodov* v. *United States*, *supra*. In *Slodov*, an individual purchased the stock and assumed the management of three businesses on January 31, 1969. The new owner knew that withholding taxes due on that date had not yet been paid, but he was falsely informed by the sellers that sufficient funds remained in various business bank accounts to cover the tax liability. In fact, "at the time that [Slodov] assumed control, the corporations had no liquid assets, and whatever trust-fund taxes had been collected prior to [Slodov's] assumption of control had been dissipated." 436 U.S at 242. The new owner thereafter deposited some of his personal funds into the business and, over the next few months, the corporations acquired sufficient new funds to pay the delinquent taxes. Instead of discharging the preexisting tax debt, however, the new owner used these newly-acquired funds to pay other expenses.

The Court concluded in *Slodov* that, on these facts, the new owner was not personally liable to assure payment of the tax obligations that accrued before he became owner of the company. In reaching that conclusion, the Court first explained that Section 6672, which applies to "[a]ny person required to collect, truthfully account for, and pay over any tax" (26 U.S.C. 6672(a)), does not require a person to perform all *three* tasks before being subject to liability for withheld taxes. This Court noted (436 U.S. at 247):

> Sections 6672 and 7202 were designed to assure compliance by the employer with its obligation to withhold and pay the sums withheld, by subjecting the employer's officials responsible for the employer's decisions regarding withholding and payment to civil and criminal penalties for the employer's delinquency. If § 6672 were given petitioner's construction, the penalties easily could be evaded by changes in officials' responsibilities prior to the expiration of any quarter.

See also *Brown* v. *United States*, 591 F.2d 1136, 1140 (5th Cir. 1979). The Court concluded instead in *Slodov* only that Section 6672 does not apply when, as in that case, the funds representing the trust fund taxes had been dissipated by the prior management and the corporation had no available liquid assets with which to satisfy the tax delinquency at the time that the new owner acquired the company. 436 U.S. at 259-260.

As the court of appeals correctly explained (Pet. App. A9-A11), neither the reasoning nor the holding of *Slodov* aids petitioner in this case. Unlike the situation in *Slodov*, no delinquent obligation to pay over withheld taxes existed when petitioner took over as

president in January 1991, for the taxes were not due to be paid until the end of that month (*id.* at A10). Moreover, the funds that came into the company's possession during January 1991 were not "after-acquired" funds of the type involved in *Slodov*, for they were earned and received before the tax payment came due. See, *e.g.*, *Brown* v. *United States*, 591 F.2d at 1140. Petitioner was obligated to use all available funds in the company's possession in January 1991 to satisfy the withholding tax liability that existed at that time. These funds were more than sufficient to satisfy the company's obligation (Pet. App. A10). Petitioner, however, willfully directed that other creditors be paid instead (*id.* at A9).

4. Petitioner further errs in asserting (Pet. 12-22) that the decision of the court of appeals in this case conflicts with the holdings of other circuits. As petitioner candidly acknowledges, however, "no [other] appellate case addresses these exact facts" (Pet. 4). The decisions that petitioner cites do not hold that a person who assumes control of a corporation *before* the date on which the taxes were required to be paid over to the government has no obligation to use the funds received by the corporation prior to the payment due date to satisfy the tax obligations.[2] There

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[2] See, *e.g.*, *Jones* v. *United States*, 60 F.3d 584, 588 (9th Cir. 1995); *Muck* v. *United States*, 3 F.3d 1378, 1381 (10th Cir. 1993); *Kinnie* v. *United States*, 994 F.2d 279, 285 (6th Cir. 1993); *Denbo* v. *United States*, 988 F.2d at 1034; *Honey* v. *United States*, 963 F.2d 1083, 1088-1089 (8th Cir. 1991), cert. denied, 506 U.S. 1028 (1992); *Davis* v. *United States*, 961 F.2d 867, 872-875 (9th Cir. 1992), cert. denied, 506 U.S. 1050 (1993); *Vespe* v. *United States*, 868 F.2d at 1334 n.7; *Thibodeau* v. *United States*, 828 F.2d 1499, 1506 (11th Cir. 1987); *Purdy Co.* v. *United States*, 814 F.2d 1183, 1190 (7th Cir. 1987); *Wood* v.

is thus no conflict among the circuits on the factually distinct issue presented in this case.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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United States, 808 F.2d 411, 415-416 (5th Cir. 1987); *Garsky* v. *United States*, 600 F.2d 86, 91 (7th Cir. 1979); *Kizzier* v. *United States*, 598 F.2d 1128, 1134 (8th Cir. 1979); *Mazo* v. *United States*, 591 F.2d at 1157.